IN THE

Supreme Court of the United States

October Term, 1976

No. 76-3931

RICHARD J. O'CONNOR,

Petitioner,

v.

THE STATE TAX COMMISSION OF THE STATE OF NEW YORK,

Respondent.

PETITION FOR WRIT OF CERTIORARI TO THE COURT OF APPEALS OF THE STATE OF NEW YORK

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RICHARD J. O'CONNOR,

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THE STATE TAX COMMISSION OF THE STATE OF NEW YORK,

Respondent.

PETITION FOR WRIT OF CERTIORARI TO THE COURT OF APPEALS OF THE STATE OF NEW YORK

Petitioner respectfully prays that a Writ of Certiorari issue to review the Order of the New York State Court of Appeals entered in this case on June 17, 1976; or alternatively, the Court of Appeals having refused to hear this case, that said Writ issue to the New York State Supreme Court, Appellate Division, Third Department, being the highest Court of the State in which a decision could be had pursuant to 28 USCA 1257 (3), upon which this Court's possible jurisdiction is based.

Opinions Below

The Order of the New York State Court of Appeals denying Petitioner's motion to vacate its Order dismissing Petitioner's appeal is appended at Appendix A, p. 1a.

The New York Court of Appeals' Order of Dismissal of Petitioner's appeal is appended at Appendix B, pp. 2a, 3a.

The opinion of the New York Supreme Court, Appellate Division, Third Department, is appended at Appendix C, pp. 3a, 4a.

The opinion of the New York Supreme Court, Special Term, is appended at Appendix D, pp. 5a-7a.

The opinion of the New York State Tax Commission is appended at Appendix E, pp. 8a-11a.

Federal Jurisdiction

This appeal is brought by Writ of Certiorari pursuant to 28 USCA 1257 (3) and Article 3, Sec. 2, Clause 1 of the U. S. Constitution where the validity of a State Statute is drawn in question.

The issue raised in this case is whether or not the professional exemption to the New York State Unincorporated Business Tax as contained in Sec. 703 (c) of the New York State Tax Law and as implemented by Reg. 203.11 of the New York State Tax Commission is unconstitutional as a denial of due process and the equal protection of the law under the Fourteenth Amendment to the U. S. Constitution.

Question Presented

The exclusion of Petitioner by the Respondent from the professional exemption to the New York State Unincorporated Business Tax is arbitrary and unfair discrimination without due process of law and a denial of the equal protection of the law.

Statutes and Regulations Involved

This case involves Section 703 (c) of the New York Tax Law which prescribes an exemption to the New York Unincorporated Business Tax and can be found at p. 421 of *59 McKinney's Consolidated Laws of N. Y. Annotated* and reads as follows:

> "(c) Professions.—The practice of law, medicine, dentistry or architecture, and the practice of any other profession in which capital is not a material income producing factor and in which more than eighty per centum of the unincorporated business gross income for the taxable year is derived from personal services actually rendered by the individual or the members of the partnership or other entity, shall not be deemed an unincorporated business."

Also involved in this case is Regulation 203.11 (b) (1) of the New York State Tax Commission, 20 NYCCR Section 203.11 (b) (1), the provisions of which are set out at Appendix F, pp. 12a-14a.

Petitioner's constitutional challenge is that his exclusion from the exemption and the inclusion of attorneys and other professions is discriminatory and a denial of due process and the equal protection of the law under the Fourteenth Amendment to the United States Constitution.

Statement of Facts

1. Petitioner is a duly licensed "independent adjuster" of insurance claims for insurance carriers pursuant to Section 123 of the New York State Insurance Law.

2. He timely filed his personal income tax returns for the years 1967-1970 inclusive. The Respondent has assessed unincorporated business tax deficiencies for the years in question totalling $3,786.82.

3. Capital is not a material income producing factor and all of his income is derived from personal services.

4. Petitioner has an office in his home for record keeping only, does not advertise and has no employees but does utilize a trade name "Chautauqua Claims Service" which appears on his stationery.

5. Petitioner has timely filed the required surety bond of $1,000 annually and paid the required $25.00 license fee, as an Independent Adjuster. A copy of the required surety bond and application for a license are a part of the record in this case. From 1949-62, Petitioner was employed by insurance companies as an adjuster and became licensed as an Independent Adjuster in 1962.

6. Petitioner seeks to render his opinions to insurance carriers in an objective manner. Upon receipt of an assignment, he will talk to the insured, to various claimants and to witnesses. Based on his findings, Petitioner gives a factual appraisal of the situation and an opinion as to the carrier's liability. He also appears in behalf of the insurers at Workmen's Compensation hearings.

7. Petitioner has attended the University of Buffalo for 2-1/2 years and has taken night courses. He does not have a Bachelors Degree from any college or university.

8. Petitioner is a member of his local claimsmen's association and is subject to adhering to principles and rules of conduct, a copy of which are a part of the record.

9. Professional liability insurance is available to independent adjusters, a copy of a typical insurance policy being a part of the record.

Timeliness of Raising Federal Question in the Proceedings Below

Throughout this proceeding, commencing with its initial thirty day protest to the Unincorporated Business Tax assessment by the Respondent and which protest was dated September 20, 1972, Petitioner has consistently and timely raised his constitutional objections to his being excluded from the professional exemption. Petitioner further explicitly raised his objections in his opening statement and in his summation at the formal hearing before Respondent's examiner held on November 15, 1973.

The specificity of Petitioner's constitutional objections are recited in the opinion of the State Tax Examiner found in Appendix E of this Petition at pp. 8a-11a.

On the Petitioner's constitutional objections, the State Tax Examiner concluded that his Commission was without jurisdiction to declare a statute unconstitutional and stated his belief that the statute was constitutional.

The constitutional objections were further raised before the Special Term of the New York Supreme Court, but were implicitly rejected in the Court's final decision in the case as appears in Appendix D of this Petition at pp. 5a-7a.

On appeal, the same constitutional objections were raised before the New York Supreme Court, Appellate Division Third Department, and were specifically denied by the Court as appears in its opinion found in Appendix C of this Petition at pp. 3a, 4a.

On further appeal and re-argument before the New York Court of Appeals, Petitioner raised the same constitutional questions, but was unsuccessful in seeking to have the Court hear the case. Initially, the Court acting *sue sponte,* by letter

of its Clerk dated January 9, 1976, had agreed to hear the case based upon a letter from Petitioner's counsel dated January 6, 1976 setting forth Petitioner's constitutional objections, both of which letters appear in Appendix G, pp. 15a-22a of this Petition.

Reasons for Granting the Writ

Petitioner contends that the professional exemption as construed by the respondent in its regulations is unconstitutional on the grounds of arbitrary and unfair discrimination in favor of attorneys and other professionals without due process of law and in denial of the equal protection of the laws to Petitioner, an independent insurance adjuster.

An examination of the pertinent New York case law and available published materials illustrates that the professional exemption here in issue was enacted by the New York State Legislature simply because professionals could not then incorporate and thereby avoid the Unincorporated Business Tax at 4-1/2% which was intended to be slightly under the State's then existing 6% Corporation Tax. It was felt that the greater advantages of doing business in the corporate form justified the higher corporate rate (See Appendix H, pp. 23a, 24a containing excerpts of New York Governor Herbert Lehman's Message to the State Legislature in 1935; and Appendix I, pp. 25a, 26a, containing further comment on the legislation).

The New York State Court of Appeals addressed itself to this question in the leading case of *People ex rel. Tower et al. v. State Tax Commission,* 282 NY 407, 408 (1940) as follows:

> ". . . the Legislature chose to exempt the professions of the law, medicine, dentistry and architecture for the express reason that under existing law, they cannot be conducted under corporate structure . . ."

Respondent agreed through its legal counsel in its own Tax Bulletin, 1968 NYTB, v. 1, pages 57-8, issued January 1, 1969:

> "The reason why the legislature provided that the practice of law, medicine and other professions shall not be subject to the Unincorporated Business Tax was that corporations cannot practice these professions, so that individuals who do practice them are not in competition with corporations which are required to pay a corporation franchise tax."

By Article 15 of the Business Corporation Law enacted May 19, 1970, (*6 McKinney's Consolidated Laws of New York Annotated,* p. 53 of Supplement) the state-wide barrier to professionals incorporating was removed. In so doing, petitioner contends that the continuation of the professional exemption under Sec. 703 (c) of the New York Business Corporation Law at the same time that respondent assesses the tax to petitioner is unfair discrimination without due process of law against the petitioner and a denial to him of the equal protection of the law in violation of the Fourteenth Amendment to the United States Constitution.

Consistently the Courts have inquired into the intent of the legislature in interpreting statutes. The Courts have recognized that the basis for tax exemptions must

> ". . . rest on real and not feigned differences, that the distinction have some relevance to the purpose for which the classification is made, and that the different treatments be not so disparate, relative to the difference in classification as to be wholly arbitrary" (Justice Jackson).

Walters v. St. Louis, 347 U.S. 231, 98 L. ed. 660, 665; 74 Set 505 (1954).

In this case, the purpose for the original professional exemption has been eliminated. To sustain the continuing

validity of the professional exemption and its presumed constitutionality is to require a judicial broadening of the classification from what has been previously stated as the intent of the Legislature. By leaving to the Courts and to the respondent the determination of what constitutes an "other profession" under Section 703 (c), the Legislature has allowed for varying interpretations. Without such a broadening interpretation to include Petitioner, the respondent's cited regulation 203.11 at Appendix G, pp. 15a-22a fails constitutionally for both due process and equal protection reasons in discriminating arbitrarily in favor of certain professionals such as attorneys and against petitioner.

The continued insistence by respondent and exclusion of petitioner from the professional exemption even in the face of the incorporation rights of professionals such as now exists leads to petitioner's conclusion that what must have been intended by the Legislature in the professional exemption was to exempt those categories who in practical fact "would" not incorporate as opposed to those who "could" not incorporate. Petitioner, like most attorneys, is so situated that he would not incorporate. The primary reason for this is that he basically has nothing transferrable by sale or inheritance because his services are personal in nature. Therefore, there are no corporate advantages in perpetual existence and ready transferability of shares of stock.

The personal service standards contained in the statute do require that success in any of the enumerated professions as well as that of petitioner is a matter of talent and individual characteristics. As stated above, whatever value there is to a law practice or to petitioner's claim service at death is of little or no value and is not transferrable. This is generally true of all businesses where capital is not a material income

producing factor and income is derived exclusively from personal services. (*Estate of Arthur J. Brandt,* 8TCM 820, P-H TC memo 49, 226, page 728 [1949]).

It is significant to note that the New York licensing statute applicable to petitioner specifically excludes attorneys from compliance with its terms at Section 123 (6)(c) of the Insurance Law.

> "6. Nothing contained in this section, and applicable to independent adjusters, shall apply to: (c) any licensed attorney at law of this State." (*27 McKinney's Consolidated Laws of N.Y. Annotated,* p. 307.)

This is at the heart of petitioner's case. All of petitioner's work is done by attorneys.

The recent case decided by the New York Court of Appeals in *Matter of Koner v. Procaccino et al.,* (39 NY 2d 258, 383 NYS 2d 295, decided April 1, 1976) is illustrative of the arbitrariness to which the professional exemption and its interpretive regulation are subject. This case held that self-employed photographers are not to be treated equally to artists and musicians which are recognized (*Voorhes v. Bates,* 308 N.Y. 184 [1954]) as being exempt from the tax—the *Voorhes* case establishing that neither professional licensing nor advanced degrees were required for the exemption (See the dissent of Justice Fuchsberg in the *Koner* case at 383 N.Y. 2d 295, 299). Industrial designers have also been found to be exempt (*Matter of Teague v. Gray,* 261 AD 652, affirmed 287 NY 549 [1941]). A landscape architect without a graduate degree has similarly been found entitled to the exemption (*Matter of Geiffert v. Mealey,* 293 N.Y. 583 [1944]).

The removal of the barrier of incorporation combined with the various Court interpretations that do not require any

professional license or advanced degree result in a maze on contradiction and often tortuous reasoning by the Courts in order to sustain the exemption. This Court should either void the exemption without further delay or to sustain it constitutionally should include this petitioner within it.

To further confuse the situation, the continuation of the State-wide professional exemption is now in direct contrast to the situation of professionals in conducting their business in New York City. In 1966, Chapter 772 of the Laws of the State of New York was enacted "to enable any city having a population of one million or more to raise tax revenue by authorizing the imposition of taxes . . . on unincorporated businesses." Specifically excluded from such definition was the same professional exemption which is still contained in the state-wide law *(McKinney's 1966 Session Laws of New York, Chapter 772, page 941 and Sec. 103 of City Unincorporated Business Income Tax at page 1061).*

Pursuant to Chapter 772, New York City enacted its City Unincorporated Business Tax making it applicable to income beginning with the calendar year 1966 and adopting the language of Chapter 772 to define the tax and exemptions therefrom.

On June 9, 1971, Chapter 412 of the Laws of the State of New York was enacted to allow New York City to repeal the professional exemption. New York City followed Chapter 412 with the enactment of its own local law No. 36 and adopted the language of the Legislature (*McKinney's 1971 Session Laws of New York, Chapter 412, pages 594-595*).

Many New York cases followed raising the issue of whether or not the repeal of the professional exemption by the State Legislature was unconstitutional. One of these cases was

Shapiro v. City of New York, 67 Misc. 2d 1021; affirmed 32 NY 2nd 96 (1973). Upon review of the Court's opinion, it appears that respondent very likely used this Petitioner's same argument to justify the repeal of the professional exemption at 325 NYS 2d 787, 791:

> "This Court will not determine plaintiff's application on the narrow ground that since members of the professions may now incorporate the repeal of the exemption may not be assailed."

Moreover, the United States Supreme Court has seen fit to refuse to grant a special exemption to the learned professions from the restraint of trade provisions in Section 1 of the Sherman Anti-trust Act. *15 U.S.C. 1.* Accordingly, attorneys' minimum fee schedules were found to be illegal in restraint of trade and commerce under the federal Sherman Anti-trust Act. (*Louis H. Goldfarb et ux. v. Virginia State Bar Association,* .... U.S. ...., 44 L.ed. 2d 572, 95 S.Ct. .... 1975).

Among the alternative remedies presented to this Court could very well be a holding of the professional exemption to be unconstitutional, leaving the balance of the tax law in effect and allowing to petitioner his claim of not being liable for tax to date, but decreeing that hereafter petitioner and all persons similarly situated, including all professionals previously exempted should be liable for the tax. By such an order, no mass refunds need be allowed for other taxpayers on the grounds of public policy involved in the substantial reliance by government on such revenues for budgetary purposes. Such a restricted remedy has been followed in criminal cases before the United States Supreme Court which raised the issue of retroactive application of a statute held unconstitutional (See *Desist v. United States,* 394 U.S. 244, 89 S.Ct. 1030, 22 L ed. 248 [1969]).

The injustice benefitting professionals, including attorneys, in our basically classless society would thereby be removed by the legal system itself at a time when the public is often reckless in its criticism of the legal system and the many excellent judges and lawyers forming its backbone. This extra judicial consideration is described for background purposes only and is relevant on the issue of the retrospective application of the unconstitutional statute as discussed by the U. S. Supreme Court in the *Desist* case cited above.

Conclusion

For the reasons stated above, this Petition for Certiorari should be granted.

Respectfully submitted,

H. JAMES ABDELLA,
Johnson, Peterson, Tener
& Anderson,
Bankers Trust Building,
Jamestown, New York 14701,
(Attorneys for Petitioner).

APPENDIX A

Opinion and Order of New York State Court of Appeals, Motion No. 612, Decided June 17, 1976

STATE OF NEW YORK
COURT OF APPEALS

Mr. Zolezzi

At a session of the Court, held at Court of Appeals Hall in the City of Albany on the seventeenth day of June A. D. 1976.

Present, HON. CHARLES D. BREITEL,
Chief Judge, presiding.

Mo. No. 612

In the Matter
of
the Application of RICHARD J. O'CONNOR,
Appellant,

vs.

THE STATE TAX COMMISSION OF THE STATE OF NEW YORK,
Respondent.

A motion for reargument of a motion to dismiss the appeal in the above cause having been heretofore made upon the part of the appellant herein and papers having been submitted thereon and due deliberation thereupon had, it is

ORDERED, that the said motion be and the same hereby is denied.

JOSEPH W. BELLACOSA,
Joseph W. Bellacosa,
Clerk of the Court.

APPENDIX B

Opinion and Order of New York State Court of Appeals, Motion No. 64, Decided February 19, 1976

STATE OF NEW YORK

COURT OF APPEALS

At a session of the Court, held at Court of Appeals Hall in the City of Albany on the nineteenth day of February A.D. 1976.

Present, HON. CHARLES D. BREITEL,
Chief Judge, presiding.

Mo. No. 64

In the Matter
of
the Application of RICHARD J. O'CONNOR,
Appellant,
vs.
THE STATE TAX COMMISSION OF THE STATE OF NEW YORK,
Respondent.

A motion having heretofore been made herein upon the part of the respondent to dismiss the appeal taken by the appellant in the above cause to this Court and papers having been submitted thereon and due deliberation having been thereupon had, it is

Appendix C—Opinion of New York Supreme Court Appellate Division.

ORDERED, that the said motion be and the same hereby is granted and the appeal dismissed, without costs, upon the ground that no substantial constitutional question is directly involved.

JOSEPH W. BELLACOSA,
Joseph Bellacosa,
(Seal) *Clerk of the Court.*

APPENDIX C

Opinion of New York Supreme Court Appellate Division, Third Department, Docket No. 26082, Decided November 20, 1975

SUPREME COURT
Appellate Division—Third Judicial Department

November 20, 1975 26082

In the Matter
of
RICHARD J. O'CONNOR,
Appellant,
v.
STATE TAX COMMISSION,
Respondent.

Appeal from a judgment of the Supreme Court at Special Term, entered January 28, 1975 in Albany County, which dis-

missed petitioner's application, in a proceeding pursuant to CPLR article 78, and confirmed a determination of the State Tax Commission sustaining unincorporated business tax assessments imposed under article 23 of the Tax Law.

We agree with the court's decision confirming the determination of the respondent that the services rendered by petitioner as an independent claims adjuster do not entitle him to a professional exemption under subdivision (c) of section 703 of the Tax Law (*People ex rel. Tower* v. *State Tax Commission*, 282 N.Y. 407; *Matter of Koner* v. *Procaccino*, 45 A D 2d 551; *Matter of Rosenbloom* v. *State Tax Comm.*, 44 A D 2d 69). On this record, such a finding is not arbitrary or capricious. We find no merit in petitioner's assertions that there is any constitutional violation in the statutory exemption or its application (see *Shapiro* v. *City of New York*, 32 N Y 2d 96; *People ex rel. Moffet* v. *Bates*, 276 App. Div. 38).

Judgment affirmed, without costs.

GREENBLOTT, J. P., SWEENEY, KOREMAN, MAIN and REYNOLDS, JJ., concur.

APPENDIX D

Opinion of Special Term of New York Supreme Court, Third Department, Decided January 15, 1975

STATE OF NEW YORK

SUPREME COURT—County of Albany

In the Matter
of
the Application of RICHARD J. O'CONNOR,
Petitioner,

against

THE STATE TAX COMMISSION OF THE STATE OF NEW YORK,
Respondent.

To review a determination made after a hearing in the matter of Unincorporated Business Taxes Under Article 23 of the Tax Law for the years 1967, 1968, 1969 and 1970.

(Supreme Court, Special Term, Albany County,
December 13, 1974)
(Justice John T. Casey, Presiding)

Appearances:

Johnson, Peterson, Tener & Anderson, Esqs., H. James Abdella, Esq., Of Counsel, Attorneys for Petitioner, Bankers Trust Building, Jamestown, New York 14701.

Hon. Louis J. Lefkowitz, Attorney General, Attorney for Respondent, Thomas P. Zolezzi, Esq., Of Counsel, The Capitol, Albany, New York 12224.

MEMORANDUM.

CASEY, *J.*

This is a proceeding pursuant to Article 78 of the CPLR to review a determination of the State Tax Commission, which sustained unincorporated business tax assessments imposed under Article 23 of the Tax Law.

The petitioner was assessed unincorporated business tax liability upon income derived from his activities as an independent claims adjuster. The facts as developed in a formal hearing before a hearing officer designated by the State Tax Commission are undisputed.

The petitioner is a high school graduate and attended the University of Buffalo for two and one-half years. Subsequently, he took all the insurance night courses at the Millard Fillmore College at the University of Buffalo and various correspondence courses through New Amsterdam Casualty Company. From 1949 to 1962 he was adjuster. In 1962, the petitioner obtained an independent adjuster's license from the New York State Department of Insurance. As an independent adjuster he would be contacted by an insurance agency and given an assignment. Upon receipt of the assignment, he would contact the insured and obtain a statement from him; petitioner would also contact various witnesses. Upon completion of those procedures, the petitioner would issue a written report to the insurance carrier stating his opinion as to the liability of the carrier.

The issue presented is one of law. *Koner v. Procaccino,* 45 App. Div.2d 551. There are several factors to be considered

in determining whether the activities of the petitioner constitute a profession within the meaning of Subdivision (c) of Section 703 of the Tax Law. In *Rosenbloom v. State Tax Commission,* the Appellate Division listed four such factors: (1) a long-term educational background generally associated with a degree in an advanced field of science or learning; (2) the requirement of a license which indicated sufficient qualifications have been met prior to engaging in the occupation; (3) the control of the occupation by standards of conduct, ethics and malpractice liability; and (4) the barrier to carrying on the occupation as a corporation. 44 App. Div.2d 69. With regard to the fourth consideration, the court noted that it was less significant since New York now permits professionals to incorporate. *Id.* at 71 n. In *Koner v. Procaccino,* the Appellate Division added an additional consideration, *i.e.*, the services performed must involve something more than the type of services generally performed by those in the broader categories of trade, business or occupation.

Based upon previous decisions of the Appellate Division wherein the occupations of marine insurance adjuster and real estate appraisers were denied the status of a profession within the meaning of Subdivision (c) of Section 703 of the Tax Law, the respondent State Tax Commission was not arbitrary or capricious in denying petitioner's application. Compare *Bower v. Bates,* 279 App. Div. 956 with *Adelberg v. Bates,* 278 App. Div. 606 and with *Rosenbloom v. State Tax Commission, supra.*

Petition dismissed. Submit judgment.

Dated: Troy, New York,
January 15, 1975.

APPENDIX E

Decision of New York State Tax Commission Examiner, Decided July 18, 1974

STATE OF NEW YORK

STATE TAX COMMISSION

In the Matter of the Petition
of
RICHARD J. O'CONNOR

for Redetermination of Deficiency or for Refund of Unincorporated Business Tax under Article 23 of the Tax Law for the Years 1967, 1968, 1969 and 1970.

DECISION

Petitioner, Richard J. O'Connor, has filed a petition for redetermination of deficiency or for refund of unincorporated business tax under Article 23 of the Tax Law for the years 1967, 1968, 1969 and 1970. (File No. 0-56645263). A formal hearing was held before L. Robert Leisner, Hearing Officer, at the offices of the State Tax Commission, State Office Building, Buffalo, New York, on November 15, 1973, at 9:50 A.M. Petitioner appeared by H. James Abdella, Esq. The Income Tax Bureau appeared by Saul Heckelman, Esq., (James A. Scott, Esq., of counsel).

ISSUE

Did petitioner, Richard J. O'Connor's activities as a claims adjuster during the years 1967, 1968, 1969 and 1970, con-

Appendix E—Decision of New York State Tax Commission Examiner.

stitute the practice of a profession, exempt from the unincorporated business tax?

FINDINGS OF FACT

1. Petitioner, Richard J. O'Connor, and his wife filed New York State income tax resident returns for the years 1967, 1968, 1969 and 1970. He did not file New York State unincorporated business tax returns for said years.

2. On June 26, 1972, the Income Tax Bureau issued a Statement of Audit Changes against petitioner, Richard J. O'Connor, imposing unincorporated business tax upon the income received by him from his activities as a claims adjuster during the years 1967, 1968, 1969 and 1970. In accordance with the aforesaid Statement of Audit Changes, it issued a Notice of Deficiency in the sum of $3,786.82.

3. Petitioner, Richard J. O'Connor, attended the University of Buffalo for two-and-a-half years. He took night courses in insurance at the Millard Fillmore College at the University of Buffalo. He took a correspondence course through New Amsterdam Casualty Company. From 1949 to 1962, petitioner was an adjuster. Since 1962, he has been licensed by the New York State Insurance Department as an independent claims adjuster.

4. In his activities as an independent claims adjuster during the years 1967, 1968, 1969 and 1970, petitioner, Richard J. O'Connor, received assignments from insurance carriers. Upon receipt of an assignment, he talked to the insured, various claimants and witnesses. Based on his findings,

petitioner then gave the insurance carrier a factual appraisal of the situation and an opinion as to the carrier's liability. Petitioner's activities required some knowledge of the law, particularly negligence law.

5. Petitioner, Richard J. O'Connor's income as an independent claims adjuster during the years 1967, 1968, 1969 and 1970, was derived solely from personal services rendered. Capital was not a material income producing factor. Petitioner did not advertise, had no employees and had an office in his home for record keeping only.

6. Petitioner, Richard J. O'Connor, contends that in his activities as a claims adjuster, he renders objective opinions to his clients in the same manner as attorneys. He further contends that there is so much similarity between the services of attorneys and his own work that under the equal protection guarantees of the State and Federal constitutions he is entitled to the same exclusion from the unincorporated business tax that is afforded to attorneys and other professionals. Finally, petitioner contends that his exclusion from the category of a professional is arbitrary and represents unreasonable and unfair discrimination without due process of law, in violation of Article 1, section 6 of the New York State Constitution and the Fourteenth Amendment of the U. S. Constitution.

CONCLUSIONS OF LAW

A. That the activities of petitioner, Richard J. O'Connor, as a claims adjuster during the years 1967 through 1970, although requiring special knowledge and experience, did not

constitute the practice of a profession exempt from the unincorporated business tax under section 703(c) of the Tax Law. *Ottis v. Graves*, 259 A.D. 957, (insurance broker); *Bowser v. Bates*, 279 A.D. 956, (adjuster of marine losses).

B. That the State Tax Commission is without jurisdiction to declare a statute unconstitutional, but is of the belief that the statute in question is neither unconstitutional nor in violation of the "equal protection" clauses of the State and Federal constitutions.

C. That the petition of Richard J. O'Connor is denied, and the Notice of Deficiency issued June 26, 1972, is sustained.

D. Pursuant to the Tax Law, interest shall be added to the amount due until paid.

Dated: Albany, New York,
July 18, 1974.

STATE TAX COMMISSION

(ILLEGIBLE) PROCACCINO,
Commissioner,

(Seal)

A. BRUCE MANLEY,
Commissioner,

MILTON KOERNER,
Commissioner.

APPENDIX F

Regulation Prescribed by New York State Tax Commission at 20 NYCCR Section 203.11 (b) (1), pages 263-264

(b) *Rules and definitions.* To give effect to the foregoing, the following rules and definitions will be applied:

(1) *Other professions defined.* For purposes of this subdivision, the term "other profession" includes any occupation or vocation in which a professed knowledge of some department of science or learning, gained by a prolonged course of specialized instruction and study, is used by its practical application to the affairs of others, either adivising, guiding or teaching them, and in serving their interests or welfare in the practice of an art or science founded on it. The word profession implies attainments in professional knowledge as distinguished from mere skill and the application of knowledge to uses for others as a vocation. The performing of services dealing with the conduct of business itself, including the promotion of sales or services of such business and consulting services, does not constitute the practice of a profession even though the services involve the application of a specialized knowledge.

The Tax Commission presently recognizes the following as professions (in addition to the specific professions of law, medicine, dentistry and architecture, previously referred to):

Public Accountancy;
Certified Shorthand Reporting;
Chiropody and Podiatry;
Chiropractic;
Dental Hygiene;
Osteopathy;
Pharmacy;
Physiotherapy;
Certified Social Work;
Veterinary Medicine and Surgery;
Professional Engineering and Land Surveying;
Nursing;
Optometry (Ophthalmic Dispensing);
Psychology;
Landscape Architecture;
Teaching.

Appendix F—Regulation Prescribed by New York State Tax Commission at 20 NYCCR Section 203.11 (b)(1), pages 263-264.

Representations made by or on behalf of other occupations or vocations will be weighed by the Tax Commission when presented. The fact that an occupation has been designated and regulated as a profession under the Education Law will be one of the facts considered in determining whether or not such occupation or vocation constitutes a profession within the intent and meaning of section 703(c) of the Tax Law. Likewise, where the taxpayer represents that he is engaged in a professional occupation which is, or is similar to, an occupation designated as a profession under the Education Law, the compliance with or the failure to comply with the licensing requirements, or any of the other requirements of the Education Law will be one of the facts considered in determining whether or not the taxpayer's activities are in fact professional activities with the intent and meaning of section 703(c) of the Tax Law. Furthermore, the fact that the taxpayer (or, if a partnership, each of the members thereof) has or has not met the educational requirements for licensing under the Education Law would be considered by the Commission in ascertaining whether the taxpayer's activities are the result of knowledge gained by a prolonged course of specialized instruction and study necessary for the practice of the alleged profession.

Appendix F—Regulation Prescribed by New York State Tax Commission at 20 NYCCR Section 203.11 (b)(1), pages 263-264.

Musicians and artists are also recognized as professions by the Tax Commission. However, an activity which, for example, consists of executing drawings or illustrations for commercial advertising purposes, or the production of musical or dramatic shows, or the creation of advertising messages set to music is not a professional activity since it deals with the conduct of business itself.

APPENDIX G

Letter to Clerk of New York Court Of Appeals Dated January 6, 1976 and Reply of the Clerk Dated January 9, 1976

LAW OFFICES

Johnson, Peterson, Tener & Anderson

January 6, 1976

Mr. Joseph W. Bellacosa
Clerk of the Court
New York State Court of Appeals
Eagle Street
Albany, New York 12207

Re: O'Connor v. State Tax Commission

Dear Mr. Bellacosa:

This is to reply to your letter of December 29, 1975 and the jurisdictional question raised by you.

Although I do not have direct access to Cohen and Karger, *Powers of the New York Court of Appeals* (Rev. ed., 1951), I have reviewed a paraphrase of the key points from that reference described in the commentary to C.P.L.R. 5601 (b)(2), McKinney's *Consolidated Laws of New York Annotated,* p. 499.

Regarding our having raised the question below, beginning with the Appellant's protest to the State Tax Commission, through the hearing before the State Tax Examiner, in brief and in argument at Special Term, Albany County, (Hon.

Appendix G—Letter to Clerk of New York Court of Appeals Dated January 6, 1976 and Reply of the Clerk Dated January 9, 1976.

Justice John T. Casey, presiding), and in brief and in argument before the Appellate Division of the Third Department, the Appellant's constitutional objections have been consistently raised to the professional exemption under the State's unincorporated business tax in Section 703 (c) of the Tax Law.

The sole question contained in Petitioner's brief in the Appellate Division was as follows:

> "Pursuant to C.P.L.R. 7803 (3), is the exclusion of the Petitioner-Appellant by the Respondent from the professional exemption to the unincorporated business tax arbitrary and unfair discrimination without due process of law and the denial of the equal protection of the law in violation of the constitutions of the United States and the State of New York?"

As to the substantial nature of Appellant's constitutional question, I respectfully submit that the Court is presented with an extremely timely and important opportunity to remedy a wrong done to this Appellant and many other similarly situated taxpayers in this State and to at the same time provide this State with additional, much needed, revenues. Simply stated as much as possible, Appellant contends that the professional exemption as construed by the State Tax Commission in its regulations is unconstitutional on the grounds of due process and in denial of the equal protection of the laws in view of the recent enactment of laws allowing professionals to incorporate (effective May 19, 1970), when, in fact, the Legislature originally enacted the

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professional exemption solely because corporations could not engage in these professions. Therefore, since the State's corporation franchise tax was not then applying to competitors of professionals, the Legislature also exempted professionals from the Unincorporated Business Tax.

The New York State Court of Appeals addressed itself to this question in the leading case of *People ex rel Tower et al v. State Tax Commission* 282 NY 407, 411 26NE2d 955 (1940):

> "...The Legislature chose to exempt the professions of the law, medicine, dentistry and architecture for the express reason that under existing law, they cannot be conducted under corporate structure..."

Respondent agreed through its legal counsel in its own Tax Bulletin, 1968 NYTB, V. 1, pp. 57-8, issued January 1, 1969:

> "The reason why the Legislature provided that the practice of law, medicine and other professions shall not be subject to the unincorporated business tax was that corporations cannot practice these professions, so that individuals who do practice them are not in competition with corporations which are required to pay a corporate franchise tax."

Among the alternative remedies presented to this Court could very well be a holding of the professional exemption to be unconstitutional, leaving the balance of the tax law in effect, and allowing to Appellant his claim of not being liable for tax up to date but decreeing that hereafter Appellant and all persons similarly situated including all professionals previously

Appendix G—Letter to Clerk of New York Court of Appeals Dated January 6, 1976 and Reply of the Clerk Dated January 9, 1976.

exempted should be liable for the tax. By such an order, no mass refunds need be allowed for other taxpayers on the grounds of public policy involved in the substantial reliance by government on such revenues for budgetary purposes. Such a restricted remedy has been followed in criminal cases before the United States Supreme Court which raised the issue of retroactive application of a statute held unconstitutional. See *Desist v. United States* 394 U.S. 244, 89 S.Ct. 1030, 22 L.Ed.2d 248 (1969).

The additional tax revenues available to the State are obviously much needed. Federal revenues from the State would be reduced by the extra tax deduction available at a time when all New York State residents are aware of the disproportion of Federal taxes paid in return for smaller Federal revenues received by the State. An injustice benefitting professionals (including attorneys) in our basically classless society would be removed by the legal system itself at a time when the public is often reckless in its criticism of the legal system and the many excellent judges and lawyers forming its backbone. The foregoing extrajudicial considerations are described for background purposes only in the light of the Court of Appeals requiring a "substantial" constitutional question. These matters are also relevant on the issue of the retrospective application of an unconstitutional statute as discussed by the U.S. Supreme Court in the *Desist* case cited above.

To me, this has been a substantial constitutional question from the first time the issue was presented to me by my client.

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I was aware that past court cases were staked against us, but thought and have concluded that no previous case has specifically raised the constitutional issue presented in this case partly because the professional corporation laws have only been recently enacted.

Alternatively, Appellant contends that if the Court is to sustain the statute constitutionally, then in view of that recent professional corporation enactments, it must include Appellant in the professional exemption without regard to any Court precedents. Such a broadening of the professional exemption could be construed by the Court in order to constitutionally sustain the exemption but constitutionally invalidating the Respondent's regulations interpreting them. (Reg. Sec. 203.11 at 1 *CCH N.Y. Tax Reporter*, para. 19-513.) Here again, Appellant contends that the constitutional question is substantial for the reasons cited above.

In conclusion, I took this case primarily because of an element present in it which I believe to be valid—and that is that common sense and the moral side of this case dictate that given the present state of the New York State Business Corporation Law allowing professionals to incorporate and the original cited basis for the professional exemption, it is now unconstitutionally wrong in these United States of America to allow the professional exemption as heretofore interpreted by the Courts and the Respondent.

If the Court wishes to have me appear personally to discuss these matters on the jurisdictional issue, I will do so.

The enclosed copies are for your convenience.

Appendix G—Letter to Clerk of New York Court of Appeals Dated January 6, 1976 and Reply of the Clerk Dated January 9, 1976.

I assume that my motion set down for January 12, 1976 will be adjourned pending the resolution of the jurisdictional question.

Respectfully submitted,

H. JAMES ABDELLA
H. James Abdella

HJA/bb
Enclosure 10

Appendix G—Letter to Clerk of New York Court of Appeals Dated January 6, 1976 and Reply of the Clerk Dated January 9, 1976.

STATE OF NEW YORK
COURT OF APPEALS

(Seal)

Joseph W. Bellacosa
Clerk of the Court

Clerks Office
Albany 12207

January 9, 1976

H. James Abdella, Esq.
Johnson, Peterson, Tener & Anderson
Bankers Trust Building
Jamestown, New York 14701

Re: O'Connor v. State Tax Commission

Dear Mr. Abdella:

Thank you for responding to the Court's inquiry in this manner.

Please be advised that this appeal will continue in its normal course and the Court will not act *sua sponte*.

This letter does not represent an adjudication of the subject matter jurisdiction and is without prejudice to a consideration of that question by the Court at the time of oral argument.

Very truly yours,

JOSEPH W. BELLACOSA
Joseph W. Bellacosa

JWB:im

cc: Thomas P. Zolezzi, Esq.,
Assistant Attorney General

Appendix G—Letter to Clerk of New York Court of Appeals Dated January 6, 1976 and Reply of the Clerk Dated January 9, 1976.

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cc: Thomas P. Zolezzi, Esq.,
Assistant Attorney General

APPENDIX H

Excerpts From Public Papers of New York Governor Herbert H. Lehman, Second Term 1935, pp. 107-108

UNINCORPORATED BUSINESS TAX

For many years business conducted in this State by individual proprietors and by partnerships has been favored under our tax laws as compared with business conducted under the corporate form of organization. It is proper that the State should impose a tax for the privilege of carrying on business operations under the protection of and within the social and legal framework provided by the State. But the tax should be as broad as business itself and should not be confined to corporate business alone, although as will presently be shown, a somewhat higher rate on corporations is justified. This has long been recognized and, as early as 1922, a report of the Special Joint Committee on Taxation and Retrenchment of Legislature urged that this defect in the State's tax system be repaired by abolishing the personal property tax then levied on unincorporated concerns and imposing upon their net income a business tax similar to the franchise tax on corporations but at a lower rate. That recommendation has since been repeated by every authority who has studied our tax system. Subsequently, the personal property tax was abolished but the unincorporated business tax was not enacted. In my view, it is eminently fair that a business carried on at a profit by a single proprietor or by a group of partners should pay a tax upon its net earnings corresponding to the franchise tax on business corporations.

Appendix H—Excerpts From Public Papers of New York Governor Herbert H. Lehman, Second Term 1935, pp. 107-108.

As pointed out above, however, the rate should be somewhat lower than the rate of the franchise tax on corporations. This differentiation in rate should be made in recognition of certain advantages which the corporate business enjoys. Corporations have the privilege of limited liability and various other advantages not available to unincorporated competitors. Because of this, the lower rate on unincorporated business is offered as an equitable adjustment.

The establishment of an unincorporated business tax is, in the financial emergency faced by the State, a desirable and logical tax.

Therefore I recommend that:

A temporary emergency tax to be imposed at the rate of 4 per cent for one year (1936) upon the net income in excess of $5,000 on every unincorporated business (professions excluded). This tax to be based on the earnings of such unincorporated business for the year 1935.

I estimate the yield of such a tax to be $6,500,000

APPENDIX I

Report of New York State Commission for the Revision of the Tax Laws

EXCERPT FROM NEW YORK
LEGISLATIVE DOCUMENT (1932)
Vol. 18, No. 77, pp. 183-184

Extension of Tax to Unincorporated Business

In states having a personal income tax there is a certain advantage to be gained by doing business in the corporate form, for stockholder A is not taxed on his undistributed profits in the business, whereas partner B or individual owner C is so taxed. Likewise, there are certain advantages to be gained in a business way through the corporate form, the most marked one being that of limited liability. But here it must be recalled that the corporate form is open to all commercial and industrial firms, and if any do not take advantage of it, it must be because for them these advantages are counterbalanced by certain disadvantages. Further, most non-resident ownership interest in business enterprise carried on in New York State is probably in the form of stockholdings rather than in partnership interest or individual ownership. The first and third factors above, and possibly the second, justify heavier taxation of corporate than of non-corporate earnings, but probably not to the extent that exists at present, where corporations pay a 4.5 per cent tax on net income, whereas non-corporate enterprises pay only a loosely-administered tax on stock in trade (personal property tax). Although no state yet taxes non-corporate business on net income it appears logical for New York to take this step, if an artificial advantage in favor of non-corporate enterprise is not to be established

through the taxing system. Such a change would also permit the abolition of the personal property tax, which has long been recognized as one of the weakest elements, from the points of view both of administration and principle, in the present tax system. In view of what has been said above, the rate should be somewhat lower than the corporate rate, a spread of one per cent being perhaps sufficient.